B4750-1
3/17/83

Financial Markets

Irving Trust

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Economic Research &
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Friday
(Noon)

Mar. 11, 1983

By refocusing attention on fast growing money supply, Chairman Volcker dramatically altered the tone in the money markets this past week. In testimony before the House Budget Committee, Mr. Volcker admitted that M1 had been growing more rapidly than he had anticipated, causing the Fed to keep an eye on it. This is the first time since the Chairman's testimony before the Senate Banking Committee on February 16 that Mr. Volcker has pointed specifically to M1. Indeed, in his February 16 testimony, he downgraded the importance of M1 and highlighted that of M3. The money markets reacted to this change in emphasis.

Mr. Volcker's switch to being concerned over the growth of M1 is neither unexpected nor a change in policy. Still the switch has come sooner than most would have anticipated. At this time, the thrust of the Fed's concern remains in the background: M1's growth rate is too high to be sustained in the long run, but it is expected that M1 will behave itself within the next six months. So, in his typical way, Mr. Volcker has given us two sides of the story. Yet he has also given us news: that continued strong growth of M1 would lessen the prospects for lower interest rates, and that, should the economic recovery seem strong enough, the Fed might act more aggressively to stem a fast growing M1.

Such concerns are not immediate, however. This past week's Fed activities in the money market are one indication. The last statement week was a clear large drain week for bank reserves, yet the Fed did not go into the open market to do matched sales or outright sales of government securities to reduce bank reserves. The Fed drained reserves in a very passive way. Some of the drain was effected by the Treasury's increasing its balance held at the Fed. Some of it was done by the Fed's making securities sales (matched or outright) to its customers, central banks, and other official institutions. Their payment of "cash" to the Fed constitutes the drain. The opportunity for such securities sales undoubtedly was enhanced by tensions in the currency markets abroad. Frequently, when a member currency of the European Monetary System (EMS) strengthens too much it is sold in exchange for dollars to ease pressure on the weaker currencies in the EMS. The dollar balances from the sale of the strong currency accrue to the intervening central bank and may be available for investment in U.S. Treasury securities held at the Federal Reserve Bank of New York.

The Fed's generally passive draining of bank reserves has been a continuing theme for this year. It must be read as a signal that the Fed does not want any misinterpretation of its action; it is not tightening. What is more important, however, is the quantity of bank reserves the Fed makes available to the banking system. The method by which reserves are made available can transmit a signal, but let's not get carried away with nuance.

Robert A. Brusca

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Market Yields

	3/11/83 (Noon)	Week Ago	Year Ago
Prime Lending Rate at Irving Trust Company	10.50%	10.50%	16.50%
Effective since	2/28/83		
Discount Rate at Federal Reserve Bank	8.50	8.50	12.00
Federal Funds	8.25	8.38	14.75
Repurchase Agreements	8.38	8.38	14.50
U.S. Treasury Issues			
Bills			
3 months	8.54	8.21	13.18
6 months	8.72	8.39	13.74
1 year	8.96	8.59	13.87
Coupons			
2 years	9.63	9.28	14.21
4 years	9.95	9.64	14.03
7 years	10.40	10.13	14.00
10 years	10.52	10.26	13.90
Long Bond	10.66	10.44	13.60
Negotiable Certificates of Deposit-Secondary Market			
1 month	8.55	8.25	14.20
3 months	8.65	8.25	14.40
6 months	8.70	8.35	14.50
1 year	9.15	8.60	14.70
Banker's Acceptances			
1 month	8.55	8.25	14.15
3 months	8.65	8.25	14.40
6 months	8.75	8.35	14.55
Eurodollar Deposits			
1 month	9.13	8.75	15.06
2 months	9.25	8.75	15.06
3 months	9.31	8.75	15.06
Commercial Paper - Prime Names			
Directly placed by:			
Finance Companies			
1 week	8.51	8.51	14.49
1 month	8.68	8.42	14.10
3 months	8.68	8.13	13.90
Bank Holding Companies			
1 month	8.30	8.04	13.58
Dealer Placed:			
3 months	8.66	8.41	14.72
New AA Corporate Utility Bond	11.90	11.75	16.25
Tax Exempt			
6 month Project Notes	4.40	4.30	7.75
1 year AAA Bond	4.75	4.50	8.00
5 year AAA Bond	6.00	6.00	9.20
20 year AAA Bond	8.50	8.25	11.95

This information represents prevailing market yields.
It should not be construed as an offering.
All yields are on the offered side of the market.

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